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IN THE

Supreme Court of the United States

OCTOBER TERM, 1957

NO. 328

ELEANOR D. GOODMAN, Administratrix of the Estate Jacques Blum, Deceased, Petitioner

v.

STANLEY GRANGER, Collector of Internal Revenue for the 23rd Collection District of Pennsylvania

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

LOUIS CAPLAN
1122 Frick Building
Pittsburgh, Pa.
CHARLES E. KENWORTHEY
J. TOMLINSON FORT
747 Union Trust Bldg.,
Pittsburgh, Pa.
Attorneys for Petitioner

Of Counsel:
REED, SMITH, SHAW & MCCLAY

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v.

STANLEY GRANGER, Collector of Internal Revenue for the 23rd Collection District of Pennsylvania

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Petitioners pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit, reversing the judgment of the District Court for the Western District of Pennsylvania.

CITATIONS TO OPINIONS BELOW

The opinion of the United States Court of Appeals for the Third Circuit is reported in 243 F.2d 264, and is printed in the Appendix hereto p. 15 et seq. The opinion of the United States District Court for the Western District of Pennsylvania is unreported, but is printed in the Appendix hereto p. 24 et seq.

JURISDICTION

The judgment of the Court of Appeals was entered on April 12, 1957. Rehearing was denied on May 2, 1957. The jurisdiction of the Court is invoked under 28 U.S.C.A. §1254.

QUESTION PRESENTED

Are the deferred compensation payments in an employment contract that are payable if, and only if, certain contingencies are met, to be valued for Federal Estate Tax purposes at the fair market value of the interest of the deceased employee immediately before his death or at the value to the employe's estate after the deferred payments have ripened into a fixed obligation by reason of the death of the employee and the consequent removal of the contingencies?

STATUTE AND REGULATION INVOLVED

The statutory provision involved is §811 of the Internal Revenue Code of 1939 which provides:

> "Sec. 811. Gross Estate—The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—
>
> "(a) Decedent's interest. To the extent of the interest therein of the decedent at the time of his death;"

The applicable regulation involved is Regulation 105, §81.10 which provides:

"Regulation 105. Section 81.10: Valution of property. (a) *General.* The value of every item of property includible in the gross estate is the fair market value thereof at the time of the decedent's death or, if the executor elects in accordance with the provisions of section 81.11, it is the fair market value thereof at the date therein prescribed or such value adjusted as therein set forth. The fair market value is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell. The fair market value of a particular kind of property includible in the gross estate is not to be determined by a forced sale price. Such value is to be determined by ascertaining as a basis the fair market value as of the applicable valuation date of each unit of the property. For example, in the case of shares of stock or bonds, each unit of property is a share or a bond. All relevant facts and elements of value as of the applicable valuation date should be considered in every case."

STATEMENT OF THE CASE

Petitioner seeks review of the decision of the United States Court of Appeals which ruled that for the purposes of federal estate taxation certain contracts for deferred compensation should be valued as of a time *after* the decedent's death when they had ripened into fixed obligations, rather than before his death when still subject to contingencies. This decision reversed a ruling by the U. S. District Court for the Western District of Pennsylvania. The basic question raised in this case is the method of valuing assets for the purposes of federal estate taxation.

The facts are largely undisputed. For several years prior to his death, Jacques Blum was a Vice President of Gimbel Brothers, Inc. in charge of its Pittsburgh store. Although apparently in excellent health, he died suddenly and unexpectedly of a heart attack on May 2, 1947 when only 52 years old. His untimely death undoubtedly cut short a highly successful career in retailing.

On October 19, 1944 Blum entered into an employment contract with Gimbel Brothers, providing for a $50,000 a year salary plus deferred compensation in the form of "contingent payments" of $2,000 a year payable for 15 years after his employment ended. (A copy of the contract is printed in the Appendix hereto, p. 34 et seq.) The contract provided, however, that he would be entitled to this deferred compensation if, and only if, the following requirements were met:

1. Blum has devoted his best efforts and all his business time and attention to Gimbels for the duration of the contract.

2. Blum has not engaged in a competing business for two years after his employment ended in any city with a population in excess of 200,000 people, or for three years in any city where Gimbels maintains a store. Failure to meet this requirement ends all rights to these payments.

3. Contingent payments shall be eliminated or reduced to the extent necessary in order that Blum's salary from other employers plus the deferred compensation shall not be in excess of 75% of his average wage in the last three years of his employment with Gimbels.

The contract provided that the deferred compensation could be paid to Blum's personal representative upon his death.

Blum entered into identical contracts with Gimbels on June 1, 1945 and May 26, 1946 so that his possible deferred compensation totaled $6,000 a year for 15 years.

The issue was raised in an action for a refund in the U. S. District Court for the Western District of Pennsylvania.

At trial plaintiff offered testimony of three experts who had been engaged for many years in the business of buying and selling future interests. Their testimony was uncontradicted. They reported that there is a well developed market in the United States for all types of

future interests created by wills, trusts, and contracts. They had made a careful study of the contracts involved in the present action. It was their unanimous opinion that Blum's interest in them during his lifetime and until death had *no fair market* value because of the various contingencies described above.

The U. S. District Court accepted this testimony and ruled that Blum's interest in the right to the deferred compensation had no fair market value during his lifetime. The Court of Appeals reversed by ruling that this right should be valued as of a time *after* Blum's death when it had ripened into a fixed obligation.

REASONS FOR GRANTING THE WRIT

The court should grant certiorari in this case because it involves a problem of wide spread and growing importance to the administration of federal estate taxation, which the Court of Appeals decided in a way in conflict with the applicable decisions of this court.

Section 811 of the Internal Revenue Code of 1939 provides that the value of the gross estate shall be determined by including all property of the decedent "to the extent of the interest therein of the decedent at the time of his death."

The Court of Appeals did not question the finding of the District Court that so long as Blum lived his contingent rights to future payments had no market value. It ruled, however, the right to deferred compensation must be valued as of a time *after* Blum's death when it was no longer subject to the contingencies. Thus, it explained:

> "Death ripened the interest in the deferred payments into an absolute one, and death permitted the imposition of the tax measured by the value of that absolute interest in property."

Petitioner submits that this represents a fundamental misconception of the scheme of federal estate taxation.

In *Knowlton v. Moore,* 178 U. S. 41, which involved the constitutionality of a federal estate tax appearing in the War Revenue Act of 1898, the court by Mr. Chief Justice White stated at p. 49:

> "What it taxes is not the interest to which some person succeeds on at death, but the interest

which ceased by reason of the death. Unless this principle is kept clearly in view, the mind is constantly tempted by the wording of the act to revert to principles of succession duty which have no real connection with the subject."

In *Young Men's Christian Association v. Davis*, 264 U.S. 47, the Court said in speaking of federal estate taxes at p. 50:

> "What was being imposed here was an excise upon the transfer of an estate upon death of the owner. It was not a tax upon succession and receipt of benefits under the law or the will. It was death duties as distinguished from a legacy or succession tax. What this law taxes is not the interest to which the legatees and devisees succeeded on death, but the interest which ceased by reason of the death. Knowlton v. Moore, 178 U. S. 41, 48, 49, 44 L. Ed. 969, 972, 973, 20 Sup. Ct. Rep. 747."

Similarly in *Edwards v. Slocum*, 264 U.S. 61, the Supreme Court by Mr. Justice Holmes said in speaking of the character of federal estate taxation at p. 62.

> ". . . It taxes, as Hanson, Death Duties, puts it in a passage cited in 178 U.S. 49, 'not the interest to which some person succeeds on at death, but the interest which ceased by reason of the death.' It levies a sum equal to a certain percentage of the value of the net estate, and provides the criteria by which the net estate shall be ascertained. * * *"

In accord: *Nichols v. Coolidge*, 274 U.S. 531.

Although not dealing with deferred compensation, the Tax Court in several decisions has applied a rule

which is in conflict with the decision of the Court of Appeals in this case.

Thus, in *Harper v. C.I.R.*, 11 T.C. 717, the decedent died possessing notes which had been executed by the residuary legatees under her will, none of whom during decedent's lifetime had sufficient funds to pay them off. The Commissioner asserted that the notes for federal estate tax purposes were worth their face value, since by death of the decedent, the makers had obtained enough funds to pay the obligations in full. The court rejected this argument by saying at page 720:

> "Respondent seeks to include the notes in decedent's gross estate at face value plus interest for the reason that immediately upon the death of the decedent the makers of the notes became vested with more than sufficient assets to satisfy their obligations. In other words, he looks to the amount of the inheritances of the makers to create value in notes which otherwise had no value in excess of the security therefor plus the net worth of the makers. In doing this he overlooks the fact that the estate tax is a tax imposed 'on the privilege of transferring the property of a decedent at death, measured by the value of the interest transferred or which ceases at death.' *Chase National Bank v. United States*, 278 U.S. 327. And Section 811 of the Internal Revenue Code provides that the value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property 'to the extent of the interest therein *of the decedent* at the time of his death.' (Italics supplied). *At the time of her death the decedent had*

an interest in notes the value of which did not exceed the value of the assets held as security therefor plus the net worth of the makers, and that is the interest which ceased at her death. . . ." [Emphasis added]

In *Estate of James H. Matthews*, 3 T.C. 525, the decedent gave to a business associate an option to purchase so many shares of stock in the James H. Matthews Company as he possessed *at the time of death* for $90 per share. There was no restriction on the decedent's right to sell the stock prior to his death. Absent this option, the market value of the stock was $120 per share. Immediately after decedent's death the option was exercised.

The petitioner argued that the option price of $90 per share must be taken as the fair market value since after decedent's death no one would pay more for the stock which was subject to the option. The court rejected this argument on the ground that up to the moment of death, the decedent could sell the stock at full market value. Thus the court said at page 528:

"The option agreement was to apply only to the stock which might be owned by the decedent at the time of his death and decedent was under no obligation to retain ownership of any of the shares until his death. He was free up to the very moment of his death to sell or otherwise dispose of the shares for the best price obtainable. That right terminated with and by reason of his death. Likewise the right of the optionee to purchase the shares came into existence at the time of and by reason of decedent's death.

* * * * * * *

> "Decedent retained the full ownership of and interest in his shares until his death and *that interest ceased by reason of his death.* [Emphasis added]
>
> "The respondent has determined that the shares in question had a fair market value at the date of decedent's death, independently of the option agreement, of $120 per share, and the petitioner has offered no evidence to the contrary. The respondent's determination is therefore sustained."

Further, it has been uniformly held that an employee does not receive any taxable income under a contract providing for deferred compensation, when subject to the contingencies present in this case, until payment is actually made. *Mooney et al. v. C.I.R.*, 9 T.C. 713; *Hall v. C.I.R.*, 15 T.C. 195. Thus, the petitioner has paid and will continue to pay income taxes on the $6,000 a year payments as received.

In its opinion, the Court of Appeals does not attempt to refute these decisions or to cite any opinions in support of its conclusion that the deferred compensation contracts should be valued as of a time after death. Rather the rationale of the court was that since death is the occasion for the imposition of the tax, any value added by death should be included in the gross estate. Thus, the court said:

> "Since death is the propelling force for the imposition of the tax, it is death which determines the interest to be includible in gross estate."

Petitioners respectfully suggest that the Court of Appeals has failed to distinguished between the occa-

sion for the imposition of the tax, which is concededly death, and the property subject to tax. The decisions cited above stand squarely with the principle that even though death is the occasion for the imposition of the tax, value is to be limited to the interest of the decedent which ceased at death. The effect of the Court of Appeals decision is not to measure the value of the decedent's interest, but the value received by recipient after death. Such a decision is fundamentally inconsistent with prior decisions of this Court.

The question here involved is of special importance to the administration of federal estate taxation. The use of deferred compensation contracts has grown into a most important method of compensating corporate executives. In Lasser and Rothschild "Deferred Compensation for Executives", 33 Harv. Bus. Rev. 89 (Jan.-Feb. 1955), the authors comment:

> "On the basis of such statistics as are available, the authors' examination of proxy statements and annual reports, and a study now in process under supervision of one of the authors, we estimate that of the 1,087 companies with stock listed on the New York Stock Exchange as of July 31, 1954, over 900 (approximately 9 out of 10) have in effect some form of arrangement for deferred benefits to designated executives individually or as a group."

Many of the deferred compensation plans discussed in this article present problems identical to the one in this case. For example, the Endicott Johnson Corporation and the Texas Company are mentioned as examples of companies with plans for deferred compensation

which might be payable to the employee's estate. Lasser and Rothschild, op. cit. supra. at 93, 94.

Similarly in Rothschild and Casey "Pay Contracts with Key Men" (1953 ed.), the authors list provisions in executive employment contracts of four prominent companies (including the Gimbels contract involved in this case) providing for deferred compensation which might be payable to the employee's estate. See also description of the General Motors plan in *Mooney v. C.I.R.*, supra; Washington and Rothschild "Compensating the Corporate Executive" 1951 ed.

In sum, certiorari should be granted to clarify the federal estate tax status of deferred compensation contracts such as those involved in this case. The question presented by this petition has broad public significance, bearing as it does upon the great body of deferred compensation contracts now so generally in use, and the tax effects to the thousands of corporate executives who are employed under such contracts.

Respectfully submitted,

LOUIS CAPLAN
CHARLES E. KENWORTHEY
J. TOMLINSON FORT

APPENDIX

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

NO. 12,005

ELEANOR D. GOODMAN, Administratrix of the Estate of Jacques Blum, Deceased, *Appellee*

v.

STANLEY GRANGER, Collector of Internal Revenue for the 23rd Collection District of Pennsylvania, *Appellant*

Appeal from the United States District Court for the Western District of Pennsylvania

Argued December 20, 1956
Before: GOODRICH, KALODNER and STALEY, Circuit Judges

Opinion of the Court.

(Filed April 12, 1957)

By KALODNER, Circuit Judge

When does the federal estate tax attach?

More specifically stated, when does such tax attach to a decedent-employee's contractual right to annual deferred compensation payments from his employer, payable to his estate after his death?

That problem, of first impression, is presented by this appeal by the government from a judgment in favor of the taxpayer, Eleanor D. Goodman, administratrix of the estate of Jacques Blum, deceased, in a suit brought by her in the District Court for the Western District of Pennsylvania to recover estate taxes and interest alleged to have been erroneously assessed and collected.

The District Court, subscribing to the taxpayer's contention, concluded as a matter of law that the decedent's contractual right was to be ". . . valued during decedent's lifetime and *at the moment before death . . .*" and made the factual finding that at such moment the contractual right was "valueless", for reasons which will subsequently be discussed. In its opinion the District Court stated, "It must be admitted that if the value in the contracts is to be fixed *the moment after death*, then the Government is correct in its contention in this case." (emphasis supplied) [1]

The undisputed facts may be summarized as follows:

The decedent, Jacques Blum, for several years prior to his sudden death of a heart attack at the age of 52 on May 2, 1947, was executive vice-president of Gimbel Brothers, Inc. ("Gimbel's") in charge of its Pittsburgh store.

On October 19, 1944, June 1, 1945 and May 26, 1946, decedent entered into identical contracts of employment with Gimbel Brothers covering the years ending January 31, 1945, January 31, 1946 and January 31, 1947, respectively. Each contract provided for a basic salary of $50,000 per year, and for additional "contingent benefits" of $2,000 per year for fifteen years "after the employee ceases to be employed by the employer" by reason of death or otherwise. The post-employment "contingent payments" were to be made only if the employee duly performed the services agreed upon and did not engage in a competing business within a specified

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[1] Unfortunately, the District Court's opinion is not reported.

period after termination of his employment; and they were to be reduced if his post-employment earnings from a non-competing business plus the contingent payments exceeded seventy-five percent of his yearly average compensation under the contracts. Any of the fifteen annual contingent payments which fell due after the employee's death were to be paid to his estate, or to a nominee designated in his will.

The third contract for the period of employment ending January 31, 1947 was, by its terms, renewed on a month-to-month basis and was in effect at the time of decedent's death. At the latter time there was every prospect that he would continue to advance in his highly successful career in retailing.[2]

After the decedent's death Gimbels paid the $6,000 annual installments provided by the three separate contracts ($2,000 each) to the taxpayer in her capacity as administratrix as they became due. She filed with the

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[2]Each of the contracts provided for payment of amounts falling due after the employee's death, in the following language:

"6. Any of the fifteen (15) annual contingent payments which fall due after the death of the Employee shall be paid either (1) to such person as shall furnish evidence satisfactory to the Employer showing that under the last will and testament of the Employee or for other reason he is duly authorized in law to receive such payment, or (2) to such person as shall furnish the Employer with evidence of appointment as representative of the estate of the Employee. The receipt of any such person for such payments shall release the Employer of any further obligation in respect thereof. 'Person' as used in this Article 6 may include one or more individuals, trusts, firms or corporations."

Collector a timely federal estate tax return and included the three contracts at a value of $15,000. Upon audit of the return the Internal Revenue Agent in Charge, Pittsburgh, increased the value of the three contracts from $15,000 to $66,710.34, the present worth of $90,000, payable in equal annual installments of $6,000 a year over a period of fifteen years. The increase in the value of the contracts resulted in a deficiency of $15,958.18, including interest, which was assessed against and paid by the taxpayer, and for the recovery of which she brought the suit here involved.

At the trial the taxpayer offered the testimony of three witnesses to the effect that the three contracts created no property right having any market value in the decedent while he lived.

The government offered the testimony of one witness who testified that the deficiency assessment was based upon his conclusion that the contracts created in the decedent valuable vested interests, subject to being divested, and on that theory the contracts were considered by the government to have the marketable monetary value which it had determined and assessed.

The federal estate tax is imposed upon "the transfer" of a decedent's property. (Internal Revenue Code of 1939, sec. 810),[3] and the gross estate of the decedent is determined by including "the value at the time of his

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[3] "Sec. 810. Rate of tax—A tax equal to the sum of the following percentages of the value of the net estate (determined as provided in section 812) shall be imposed upon the transfer of the net estate of every decedent, citizen or resident of the United States, dying after the date of the enactment of this title."

death of all property" to "the extent of the decedent's interest therein." (Sec. 811(a)).[4] Treasury Regulations 105, sec. 81.10 provide that the measure of value for the purpose of determining the gross estate in federal estate taxation is the fair market value of the estate.[5]

The sum of the taxpayer's position is (1) what is taxed is "the value" of the decedent's interest in his contract that "ceased by reason of death", not the value of what is received by the recipient (the administratrix); otherwise stated, "the value" of the decedent's

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[4]"Sec. 811. Gross estate—The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

"(a) Decedent's interest. To the extent of the interest therein of the decedent at the time of his death;"

[5]"Regulation 105. Section 81.10: Valuation of property. (a) *General.* The value of every item of property includible in the gross estate is the fair market value thereof at the time of the decedent's death or, if the executor elects in accordance with the provisions of section 81.11, it is the fair market value thereof at the date therein prescribed or such value adjusted as therein set forth. The fair market value is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell. The fair market value of a particular kind of property includible in the gross estate is not to be determined by a forced sale price. Such value is to be determined by ascertaining as a basis the fair market value as of the applicable valuation date of each unit of the property. For example, in the case of shares of stock or bonds, each unit of property is a share or a bond. All relevant facts and elements of value as of the applicable valuation date should be considered in every case."

interest in his contract was to be determined as "of the moment before death."

The government's position may be summarized as follows: (1) the estate tax is measured by the value of property transferred by death and here an absolute right to the fifteen deferred compensation payments passed by decedent's death to the taxpayer inasmuch as the possibility of forfeiture was extinguished by decedent's death; (2) the government properly valued the right to the deferred compensation payments in the same manner as an annuity for a term certain, i.e. at the commuted value in accordance with the applicable Treasury Regulations.

As earlier noted, the District Court agreed with the taxpayer's view. In doing so it stated:

> "It seems clear under the authorities and the statute and the regulations that the value of the contract rights *is limited to the interest of the decedent during his lifetime.* That interest, under the testimony and by a fair preponderance of the evidence, is valueless. There was no fair market value on which to base a deficiency assessment." (emphasis supplied.)

It may be noted parenthetically that the taxpayer's testimony as to lack of value, adverted to by the District Court, was premised on the circumstance that the employment contracts specified four contingencies which, if any of them had occurred, would have forfeited the decedent's right to the deferred compensation payments.

It is clear that the decedent's interest in the employment contracts was "property" includible in his

gross estate under Section 811(a) of the Internal Revenue Code of 1939. Determination of the time when that interest is to be valued is the crux of the dispute.

We have had the benefit of thorough discussions by both the government and the taxpayer of the nature of the federal estate tax. Both parties cited Knowlton v. Moore, 178 U. S. 41 (1900); Young Men's Christian Association v. Davis, 264 U. S. 47 (1924); and Edwards v. Slocum, 264 U. S. 61 (1924). The government cited them for the proposition that the subject of the tax is neither the property of the decedent, nor the property of the legatee, but rather the transfer of assets affected by death. The taxpayer emphasizes the language in these cases which supports the theory that what is taxed is the value of the interest that ceased by reason of death, not the value of what is received by the recipient. We are in accord with both of these general axioms which aid in clarifying the nature of the federal estate tax. However, the cases cited and the principles drawn therefrom are not decisive of the question posed by this case. While the nature of the tax has been discussed in numerous Supreme Court cases, the question of the proper time to determine the nature of a decedent's interest and the value thereof requires a more particularized analysis.

The taxpayer has ignored the very nature of the tax which it is urged is dispositive of this case. True, the tax reaches the "'. . . interest which ceased by reason of the death'", Knowlton v. Moore, supra at 49, but the reference there was to the distinction between an estate tax and an inheritance tax. The inheritance tax is levied upon the individual shares of the decedent's

estate after distribution to the legatees; the estate tax is imposed upon the total estate of the decedent which is transferred to the legatees. Int. Rev. Code of 1939, Sec. 810. The estate tax has been characterized as "an excise imposed upon the transfer of or shifting in relationships to property at death." United States Trust Co. v. Helvering, 307 U. S. 57, 60 (1939). The estate and inheritance taxes have the common element of being based upon the transmission of property from the dead to the living. New York Trust Co. v. Eisner, 256 U. S. 345 (1921). In Knowlton v. Moore, supra, the Supreme Court recognized this basic principle when it said (at page 56):

> ". . . tax laws of this nature in all countries rest in their essence upon the principle that death is the generating source from which the particular taxing power takes its being, and that it is the power to transmit, or the transmission from the dead to the living, on which such taxes are more immediately rested."

Since death is the propelling force for the imposition of the tax, it is death which determines the interests to be includible in the gross estate. Interests which terminate on or before death are not a proper subject of the tax. Assets may be acquired or disposed of before death, possibilities of the loss of an asset may become actualities or may disappear. Upon the same principle underlying the inclusion of interests in a decedent's gross estate, valuation of an interest is neither logically made nor feasibly administered until death has occurred. The taxpayer's theory of valuing property before death disregards the fact that generally the estate tax is neither concerned with changes in property interests nor values

prior to death.[6] The tax is measured by the value of assets transferred by reason of death, the critical value being that which is determined as of the time of death.

As was so succinctly stated by Judge Hartshorne in Christiernin v. Manning, 138 F. Supp. 923, 925 (D. N. J. 1956):

> "There cannot be a decedent, till death has occurred. A decedent's estate is not transferred either by his will or by intestacy, till death has occurred. . . . And the decedent's interest in the property taxable is to be such interest 'at the time of his death' . . ."

Here the employment contracts provided for additional "contingent" compensation of $6,000 per year for fifteen years to be paid to Blum or his estate after the termination of his employment by reason of death or otherwise. True, the right to these payments was forfeitable upon the occurrence of any of the specified contingencies. However, forfeiture as a result of the contingencies never occurred during Blum's lifetime, and any possibility of their occurrence was extinguished by his death. Gimbels has been making and the estate has been collecting the payments provided by the contracts. Valuation of the right to these payments must be deter-

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6. Cf. Newell v. Commissioner, 66 F.2d 102 (7th Cir. 1933) for the effect of the death of a key officer and shareholder in a corporation upon the valuation of stock in the corporation included in his gross estate. Also, in valuing a partnership interest of a decedent, goodwill attributable to the decedent's personal efforts is not valued due to the decedent's loss to the partnership. Estate of Gannon, 21 T.C. 1073 (1954); Estate of Maddock, 16 T.C. 324 (1951).

mined as of the time of Blum's death when the limiting factor of the contingencies would no longer be considered. Death ripened the interest in the deferred payments into an absolute one, and death permitted the imposition of the tax measured by the value of that absolute interest in property.

In Mearkle's Estate v. Commissioner, 129 F.2d 386 (1942), we considered the proper method of valuing an annuity upon the death of the decedent which by its terms was payable to the decedent during his life and to his wife for her life. The criterion adopted was the purchase price of an annuity contract upon the life of the wife measured by her life expectancy on the date of her husband's death. There is no reference in this test to the husband's life expectancy upon the date of his death or to the joint expectancies of the decedent and his wife. See Christiernin v. Manning, supra. The value of decedent's interest in the annuity up to the time of his death is not considered, and, as in the situation here involved, death cuts off prior limiting factors.[7]

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7. In Estate of Harper, 11 T.C. 717 (1948), cited by taxpayer, there were included in decedent's gross estate notes of insolvent makers who by reason of the receipt of legacies under the decedent's will became solvent. The Commissioner valued the notes at face value. The Tax Court held to the contrary, subscribing to the view that the estate tax was "measured by the value of the interest transferred or which ceases at death", viz, the actual value of the then insolvent maker's assets. The result reached is consistent with our approach in the instant case, although the language used by the Tax Court was perhaps something less than fortunate.

Judgment.

For the reasons stated the judgment of the District Court will be reversed with directions to proceed in accordance with this opinion.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit.

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 12,005

ELEANOR D. GOODMAN, Administratrix of the Estate of Jacques Blum, Deceased

v.

STANLEY GRANGER, Collector of Internal Revenue for the Twenty-third Collection District of Pennsylvania, Appellant

On Appeal From the United States District Court For the Western District of Pennsylvania

Present: GOODRICH, KALODNER and STALEY, Circuit Judges.

Judgment.

This cause came on to be heard on the record from the United States District Court for the Western District of Pennsylvania and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the

said District Court in this case be, and the same is hereby reversed, with directions to proceed in accordance with the opinion of this Court.

Attest:

IDA O. CRESKOFF
Clerk

April 12, 1957

Opinion and Order.

OPINION

Willson, District Judge

This action is for the recovery of estate taxes and interest alleged to have been erroneously assessed and collected. Plaintiff, Eleanor B. Goodman, is the Administratrix of the Estate of Jacques Blum, who died May 2, 1947.

Jacques Blum was born May 18, 1895, and died suddenly of a heart attack on the date mentioned. Prior to the day of his death he appeared to be in excellent health. At the time of his death, he was executive head of Gimbels' Pittsburgh department store. During his lifetime, decedent had entered into three written employment contracts with Gimbel Brothers, Inc. The first covered the period of employment from February 1, 1944 to January 31, 1945; the second was for the year ending January 31, 1946; and the third for the year ending January 31, 1947. The third contract for the period of employment ending January 31, 1947 was, by its terms, renewed on a month-to-month basis and was in effect at the time of decedent's death. Each of the three contracts provided for "contingent payments" to the dece-

dent, or in the event of his death to his nominee or estate, of $2,000 per year for fifteen years. The annual installments of $6,000 are being paid by Gimbel Brothers, Inc. to plaintiff.

The payments provided by each of the three contracts were forfeitable if (1) the decedent should fail to devote his best efforts and all of his business time and attention to the affairs of Gimbels, including the affairs of subsidiary or affiliated companies if Gimbels should so elect; or (2) during the period of two years beginning with the date when the decedent ceased to be employed by the employer, the decedent engaged in a competing business in any city of the United States having a population of over 200,000, without first having procured the written consent of Gimbels; or (3) during the period of three years beginning with the date when the decedent ceased to be employed by Gimbels, the decedent engaged in a competing business in any city in which Gimbels or any subsidiary or affiliated company maintains a retail store; or (4) the decedent became employed by a noncompeting business from which his total income plus his income from the contracts exceeded 75 per cent of his average compensation under the contracts.

Plaintiff filed a timely estate tax return and included the three contracts at a value of $15,000. Upon audit of the return, the Internal Revenue Agent in Charge, Pittsburgh, increased the value of the three contracts from $15,000 to $66,710.34, being the present worth of $90,000, payable in equal annual installments of $6,000 per year over a period of fifteen years.

The increase in the value of the contracts resulted in a tax deficiency of $15,958.18, including interest, which plaintiff has paid and for the recovery of which this suit is brought.

At the trial plaintiff offered the testimony of three witnesses to the effect that the three contracts created no propery right having any market value in the decedent while he lived.

The Government offered the testimony of but one witness, who was the estate examiner for the defendant, and who testified that the deficiency assessment was based upon the conclusion of the witness that the contracts were considered by the defendant to have the marketable monetary value as determined by defendant.

Plaintiff says the only question submitted to the court in this case is the value of the contract rights possessed by the decedent and included in the computation of his estate tax liability. Plaintiff says the issue involves a determination of the fair market value of the right in the contracts, since "value" as used in the Federal estate tax laws and the term "fair market value" are synonymous terms. Plaintiff cites Treasury Regulations 105, Section 81.10, and Ithaca Trust Co. v. United States, 279 U. S. 151.

The provision of the Internal Revenue Code of 1939, as amended, reads:

"SEC. 811. GROSS ESTATE

"The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except

real property situated outside of the United States . . .

"(a) Decedent's Interest.—To the extent of the interest therein of the decedent at the time of his death; . . ."

It is noted that the value mentioned in Section 811 is the " . . . *value at the time of his death of all property*", etc. and "(a) . . . *to the extent of the interest therein of the decedent at the time of his death* . . ."

Treasury Regulations 105, Section 81.10 refers to value. The regulation states that the fair market value is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell. It provides: ". . . All relevant facts and elements of value as of the applicable valuation date should be considered in every case . . ." The regulation recognizes, in the case of stocks and bonds, at the fair market value is ordinarily the selling price. That is determined by actual sale or quoted bona fide bid and asked price.

Plaintiff's position is that the Internal Revenue Code calls for a valuation of the property rights of decedent which existed during his lifetime rather than the rights received by plaintiff as executor or legatee. Plaintiff asserts that the right in Jacques Blum to receive the $2,000 a year under each of three contracts was so speculative because resting upon his personal determinations and desires as to have no value in the open market. Plaintiff offered the testimony of three witnesses, Benjamin Byer, Harry Sanger and Samuel A. Cohen, who stated that future interests created under

wills and deeds of trust are commonly dealt in, that is, bought and sold and used as security for loans in the United States and especially in England. That was their business. They were experienced in placing values upon written instruments creating such rights. These witnesses testified generally speaking, with reference to the four contingencies which, if they occurred, or any of them, forfeited the payments. They said that because the right to the payments depended upon the personal decision of Jacques Blum during his lifetime as to whether each or all of the contingencies would become operative, there was no value in the contracts in the open market.

It is believed that under the Government's own criteria, set up in the Treasury Regulations, plaintiff has met the burden of proof that there was no market value in the three contracts at the time that decedent's death occurred. The parties were contracting for the personal services of Jacques Blum. He had a demonstrated large earning ability. His salary was $50,000 a year, plus bonuses, but he had to earn it. He was required to devote his best interests and all of his business time and attention to Gimbels. It seems obvious that because of decedent's ability and earning capacity the parties contemplated that perhaps he might engage in a competing business or become associated with a competing store in other cities, or in cities where Gimbels or any subsidiary company maintained a retail store. Such provisions indicated that the contracting parties had in mind that a competitor might induce Jacques Blum to leave Gimbels. The contract periods were for one year and thereafter from month to month. Up to

a point, Gimbels made it attractive for Blum to remain in its employ. But, under the contract Gimbels might dismiss decedent at the end of any one year and had it done so, there was no penalty attached, and in that case decedent was required to look to the forfeiture provision if he desired to take advantage of the contract payments. A better job with a competitor at twice the salary Gimbels paid decedent would forfeit plaintiff's interest in the contract. Having regard for decedent's age in 1947, his demonstrated earning capacity and future possibility as to his salary and other earnings, it appears reasonable that in the open market an investor would not regard decedent's rights under the contracts as having any monetary value.

The Government's testimony was that the interest of the decedent was vested and for that reason the assessment was made. In Black's Law Dictionary a vested interest is defined as " . . . an interest clothed with a present, legal and existing right of alienation . . . whether in possession or not, which is not subject to any condition precedent . . ." One condition precedent in the contracts in issue here was that Jacques Blum was required to expend his daily efforts on behalf of Gimbels. By simply doing nothing, the contracts were not being fulfilled. The condition precedent required personal effort and decision on his part in order to earn his salary and his bonuses and the contingent payments. However, it is not necessary to engage in an abstract discussion as to whether the contracts created vested or contingent interest or just what the interests amounted to under the law relating to future interests. The issue here is simply whether under Section 811 and the Treas-

ury Regulations the contracts had any market value on May 2, 1947. The preponderance of the evidence is with the plaintiff. Her evidence points to a lack of market value in Jacques Blum just prior to his death. The Government offered no evidence on this point, but simply relies upon a construction of the contracts which it says indicates market value at the time of decedent's death. However, the principle is well established that as a general rule positive testimony as to a particular fact, uncontradicted by anyone, should control the decision of the court, unless there be an inherent improbability in the statements of a witness as to induce the court to disregard his evidence, even in the absence of any direct conflicting testimony. See a recent discussion as to the weight of uncontradicted evidence in Benton v. Blair, 228 F. 2d 55.

The issue here is one of value and marketability, as Justice Holmes stated it, ". . . But the value of property at a given time depends upon the relative intensity of the social desire for it at that time, expressed in the money that it would bring in the market . . ." Ithaca Trust Co. v. United States, supra. A reference to Knowlton v. Moore, 178 U. S. 41, seems to fortify plaintiff's contention. The language there is: ". . . . What it taxes is not the interest to which some person succeeds on a death, but the interest which ceased by reason of the death. Unless this principle is kept clearly in view, the mind is constantly tempted by the wording of the act to revert to principles of succession duty which have no real connection with the subject . . ." However, the Government in its brief contends that the decision in Knowlton v. Moore, supra, is in support of its conten-

tion in this case. It says that the estate tax is a tax upon the transfer of the decedent's assets at his death. The Government says also that in fairly recent cases the Supreme Court has referred to the tax as ". . . an excise imposed upon the transfer of or shifting in relationships to property at death . . ." United States Trust Co. v. Helvering, 307 U. S. 57, 60.

It is conceded in this case that the plaintiff, on the death of the decedent, acquired the right to collect $6,000 annually for fifteen years, but the analogous situation plaintiff cites in a tax court case is applicable here, Estate of Harper v. Comm., 11 T.C. 717. There decedent died possessing notes that were executed by the residuary legatees under her will. The executor included the notes in the decedent's estate at the net worth of the makers prior to the decedent's death. The Commissioner asserted an estate tax deficiency on the theory that the notes were worth their face value by reason of the fact that, at death of the decedent, the makers became vested with more than enough assets to discharge the obligations in full. The Tax Court, adopting the language of Chase National Bank v. U. S., 278 U. S. 327, held the notes could not be valued at a figure above the net worth of the makers, which was the value of the interest which ceased at the decedent's death.

It must be admitted that if the value in the contracts is to be fixed the moment after death, then the Government is correct in its contention in this case. But, if the property is valued during decedent's lifetime and at the moment before death, then the decision must be for plaintiff. It seems clear under the authorities and the statute and regulations that the value of the

contract rights is limited to the interest of the decedent during his lifetime. That interest, under the testimony and by a fair preponderance of the evidence, is valueless. There was no fair market value on which to base a deficiency assessment. Plaintiff's payment of the tax and interest because of the deficiency assessment is recoverable. Plaintiff concedes that it cannot recover the amount paid on the $15,000 valuation included by the plaintiff in the estate tax return because it failed to make claim therefor within the three year period. Plaintiff is entitled to an order for judgment. Counsel will submit an order on notice.

This opinion comprises the Findings of Fact and Conclusions of Law within the meaning of Rule 52.

(s) JOSEPH P. WILLSON,
United States District Judge.

ORDER OF COURT

NOW, April 18, 1956, the Court having filed its opinion comprising the Findings of Fact and Conclusions of Law in this case and directing the submission of an appropriate order for judgment in favor of the plaintiff, and notice of the proposed submission of this order having been given to D. Malcolm Anderson, United States Attorney, counsel for the defendant, it is ORDERED, ADJUDGED and DECREED as follows:

1. Judgment is hereby entered in favor of the plaintiff, Eleanor D. Goodman, Administratrix of the Estate of Jacques Blum, Deceased, against the defendant, Stanley Granger, Collector of Internal Revenue for the Twenty-third Collection District of Pennsylvania, in

the sum of $15,881.35, with interest thereon according to law at the rate of 6% per annum from June 27, 1951, the date of payment by the plaintiffs to the defendant of the said sum of $15,881.35, and with costs actually incurred for witnesses and fees paid to the Clerk of this Court.

2. The Court hereby certifies that there was probable and reasonable cause for the act of the defendant, the Collector of Internal Revenue, in demanding and collecting from plaintiff the Internal Revenue tax for the refund of which this judgment is entered.

(s) JOSEPH P. WILLSON

Agreement.

THIS AGREEMENT, made this 19th day of October, 1944 (to be effective as of February 1, 1944) between GIMBEL BROTHERS, INC., a New York corporation, hereinafter called the "Employer", and JACQUES BLUM, of Pittsburgh, Pa. hereinafter called the "Employee",

WITNESSETH:

1. For the purposes of this agreement:—

(a) The term "Employer" shall include Gimbel Brothers, Inc., party hereto, and any corporation successor to the business presently conducted by Gimbel Brothers, Inc.

(b) The Employee shall "cease to be employed by the Employer" when, whether as a result of resignation, dismissal, death or any other reason, he ceases to serve the Employer or a subsidiary or affiliated company on

a full time basis under this or some subsequent employment arrangement.

(c) The Employee shall be "engaged in a competing business" if, as proprietor, partner, trustee, employee or director, he is engaged or participates in the operation or management of a retail department or specialty store, which has a gross volume in excess of One Million Dollars ($1,000,000) a year.

2. The Employer agrees to employ the Employee and the Employee agrees to serve the Employer in an executive capacity similar to that in which he is currently serving, for the twelve (12) months' period commencing February 1, 1944 and expiring January 31, 1945. From February 1, 1945, employment may continue on a month to month basis until a new contract of employment is made; and if prior to June 1, 1945, no new contract is made and neither the Employer nor the Employee shall notify the other in writing that a continuance of this employment on these terms is not desired, a new employment contract shall be deemed to exist between the Employer and the Employee, the terms of which shall be identical with the terms hereof except that "1945" and "1946" shall be respectively substituted for "1944" and "1945" wherever such dates occur herein. In like manner and with the appropriate corresponding changes of dates, further such renewals of this agreement may occur.

3. Until January 31, 1945, the Employee shall devote his best efforts and all of his business time and attention to the affairs of the Employer (including the affairs of subsidiary or affiliated companies, if the Employer so elects).

4. For his services performed hereunder, the Employer shall pay and the Employee shall accept:

(a) Through January 1945, basic compensation of $4166.^{67}/_{100}$ per month, payable on the last day of each month in which such services were duly performed.

(b) At such times as may be fixed before or after January 31, 1945, such bonus or other payments, if any, as may be awarded by the Employer in its sole discretion.

(c) After the Employee ceases to be employed by the Employer, contingent payments of $2000.^{00}/_{100}$ per year for fifteen (15) years, payable on or before each January 15th, commencing with the January 15th next succeeding the date on which the Employee ceases to be employed by the Employer. The contingencies upon which such contingent payments and each of them shall be made or continued are the following:

(1) That the Employee shall have duly performed his services hereunder pursuant to Article 3 hereof, throughout the period expiring January 31, 1945;

(2) That the Employee shall not have engaged in a competing business as above defined:

(i) During the period of two (2) years beginning with the date when the Employee ceased to be employed by the Employer, in any city of the United States having a population of over two hundred thousand thousand (200,000) without having first procured the written consent of the Employer;

(ii) During the period of three (3) years beginning with the date when the Employee ceased to be employed by the Employer, in any city in which the Employer or any subsidiary or affiliated company, at the time when Employee first engages in such competing business, maintains a retail store, without having first procured the written consent of the Employer.

It is agreed that the Employee, by engaging in such competing business during the said two (2) year period, or three (3) year period, as the case may be, without having first procured the consent of the Employer in writing, will automatically forfeit all rights to any subsequent contingent payments becoming due thereafter. The Employer in such written consent, may specify the terms on which the consent is given and the amounts of subsequent contingent payments, which amounts may be less than those specified herein.

5. Contingent payments shall be eliminated or reduced to the extent necessary from time to time in order that the business earnings of the Employee, together with the contingent payment herein provided for, shall not in respect of any year exceed 75% of the yearly average of payments to the Employee described in subparagraph (a) of Article 4 in the last three fiscal years preceding the date when he shall have ceased to be employed by the Employer. "Business earnings" is defined to be the total compensation received, directly or indirectly, as an employee or officer of a business organization other than the Employer. The Employee

shall furnish to the President of the Employer, at his request, a certified copy of the Employee's federal income tax return and such additional information as the President of the Employer may require to assist in the determination of the amount payable to the Employee in any years under this subparagraph.

6. Any of the fifteen (15) annual contingent payments which fall due after the death of the Employee shall be paid either (1) to such person as shall furnish evidence satisfactory to the Employer showing that under the last will and testament of the Employee or for other reason he is duly authorized in law to receive such payment, or (2) to such person as shall furnish the Employer with evidence of appointment as representative of the estate of the Employee. The receipt of any such person for such payments shall release the Employer of any further obligation in respect thereof. "Person" as used in this Article 6, may include one or more individuals, trusts, firms or corporations.

7. Neither the Employee nor the estate of the Employee shall under any circumstances have any option or right to require payments hereunder, otherwise than in accordance with the terms hereof and after the terms and contingencies herein specified have been met.

WITNESS the hands and seals of the parties hereto, this 19th day of October 1944.

GIMBEL BROTHERS, INC.,
By BERNARD F. GIMBEL
[SEAL] President-Employer

JACQUES BLUM (L.S.)
Employee